

Message Text

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ACTION ARA-14

INFO OCT-01 ISO-00 MMO-01 AID-05 CIAE-00 COME-00 EB-08

FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02

OPIC-03 SP-02 LAB-04 SIL-01 OMB-01 AGRE-00 NSC-05

SS-15 STR-04 CEA-01 INT-05 ACDA-07 ITC-01 DOTE-00

DHA-02 DODE-00 /098 W

-----076168 101928Z /46

P 101745Z AUG 77

FM AMEMBASSY LIMA

TO SECSTATE WASHDC PRIORITY 6096

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E.O. 11652: N/A

TAGS: ECON, EALR, PE

SUBJECT: ECONOMIC ALERT REPORT - PERU

REF: A) STATE 180067; B) LIMA A-117; C) LIMA 4852;

D) LIMA 6379; E) LIMA 6573

1. PERU'S MAJOR ECONOMIC PROBLEMS:

A. BLANCE OF PAYMENTS CRISIS - IT IS RELIABLY ESTIMATED THAT PERU HAS \$60-100 MILLION DOLLARS IN FOREIGN OBLIGATIONS COMING DUE DURING AUGUST, AND GHE CENTRAL BANK, WITH NET RESERVES OF ABOUT NEGATIVE \$1.3 BILLION, APPARENTLY IS SCRAMBLING TO MEET FOREIGN EXCHANGE DEMANDS ON DAY-TO-DAY BASIS. (REF D). PROBABILITY OF FORCED RESCHEDULING OF FOREIGN DEBTS IN NEAR FUTURE IS HIGH. PERU NEEDS APPROXIMATELY \$300-400 MILLION IN B/P FINANCING FOR REMAINDER OF 1977. EXTERNAL DEBT SERVICE FOR 1977 IS RUNNING ABOUT 40 PERCENT OF EXPORT EARNINGS AND WILL RISE DRAMATICALLY IN NEXT FEW YEARS.

B. INFLATION - CURRENT INFLATION RATE IS MORE THAN 40 PERCENT AND OVER LAST YEAR REAL INCOME FOR WORKERS DECLINED BY SOME
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30-40 PERCENT. GOP'S MEASURES FOR SHORT TERM AMELIORATION OF WORKERS' SITUATION, HUGE PROJECTED 1977 PUBLIC SECTOR BUDGET DEFICIT (REPORTEDLY BETWEEN \$450 MILLIONA DN \$1 BILLION) AND RUMORED GOP INTENTION TO EXPAND MONEY SUPPLY (TO STIMULATE ECONOMY THROUGH INCREASED LIQUIDITY) CAN ONLY EXACERBATE INFLATIONARY SITUATION IF PURSUED.

C. RECESSION AND HIGH UNEMPLOYMENT - PERU'S GDP IS EXPECTED TO DECLINE SLIGHTLY IN REAL TERMS DURING 1977. UNEMPLOYMENT/UNDEREMPLOYMENT IS ABOUT 40-45 PERCENT.

2. OUTLOOK FOR NEXT 12 MONTHS

AS REFS C, D AND E INDICATE, UNCERTAINTY REGARDING WHAT ECONOMIC POLICIES GOP WILL FOLLOW IN WAKE OF CHANGES IN ECONOMIC TEAM AND SO-FAR UNSUCCESSFUL STANDBY NEGOTIATIONS WITH IMF MAKES IT DIFFICULT TO PROJECT TRENDS IN PERUVIAN ECONOMY OVER NEXT 12 MONTHS. GOP WILL ATTEMPT TO STRETCH OUT INTERNATIONAL LOAN REPAYMENTS WHILE AT SAME TIME STRUGGLING TO COME UP WITH A STABILITY PACKAGE TO PRESENT TO IMF (REF E). INTERNAL POLITICAL REALITIES AND GOP DESIRE AVOID FURTHER POPULAR UNREST SHARPLY RESTRICT GOVERNMENT'S MANEUVERING ROOM FOR IMF NEGOTIATIONS. BALANCE OF PAYMENTS SITUATION (AND, CONCOMITANTLY, GENERAL ECONOMIC SCENE) COULD IMPROVE CONSIDERABLY LATER IN 1978 IF LEVEL OF WORLD MINERAL AND COMMODITY PRICES RISES. ADDITIONAL FAVORABLE FACTOR WILL BE PERUVIAN PETROLEUM SELF-SUFFICIENCY (IN EARLY 1978) WITH PROSPECTS FOR SOME SMALL EXPORTS (10-20,000 BBL/DAY) WHICH WOULD REDUCE THE TRADE DEFICIT BETWEEN \$30-50 MILLION. NEVERTHELESS, EVEN UNDER MOST FAVORABLE CONSTELLATION OF EXPORT EARNINGS AND GOVERNMENT POLICY PERU WILL STILL BE STRUGGLING WITH LARGE EXTERNAL DEBT BURDEN, A SLUGGISH ECONOMY, INFLATION AND HIGH UNEMPLOYMENT. LIMITED OFFICIAL USE

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3. CRITICAL POINTS

A. EXTERNAL FACTORS - AS INDICATED ABOVE, WORLD MINERAL AND COMMODITY PRICES HAVE IMPORTANT EFFECT ON PERU'S B/P SITUATION. INTERNATIONAL FINANCIAL COMMUNITY'S POSTURE TOWARD PERU IS ALSO MAJOR ELEMENT IN OVERCOMING CURRENT CRISIS. ADDITIONAL EXOGENOUS FACTOR IS ANCHOVY CATCH, WHICH SO FAR IN 1977 HAS BEEN VERY DISAPPOINTING.

B. INVESTMENT CLIMATE - DURING LAST TWO YEARS UNCERTAINTY CAUSED BY GOP INDECISIVENESS IN ITS ECONOMIC POLICIES HAS HAD SERIOUS DETRIMENTAL EFFECT ON NEW INVESTMENT IN COUNTRY. CURRENT SENSE THAT GOP IS FLOUNDERING WITH ECONOMIC PROBLEMS HAS INCREASED THIS UNCERTAINTY NOT ONLY WITH INVESTORS BUT ALSO WITHIN INTERNATIONAL BANKING COMMUNITY. OUTLOOK DIM FOR QUICK RESTORATION OF INVESTOR CONFIDENCE.

C. PUBLIC REACTIONS - RECENT EPISODES OF VIOLENT REACTION TO ANNOUNCEMENT OF JUNE AUSTERITY MEASURES (SUBSEQUENTLY AMELIORATED IN PART) WILL INCREASE GOP'S RELUCTANCE TO IMPOSE PROGRAM DESIGNED TO MEET IMF PRESCRIPTIONS FOR UNDERLYING STRUCTURAL

PROBLEMS. THIS RELUCTANCE IS FURTHER REINFORCED BY GOP FEAR THAT EFFORTS TO CONTROL PUBLIC REACTION TO UNPOPULAR AUSTERITY MEASURES WOULD BE POLITICALLY DAMAGING WITHIN PERU AND COULD TARNISH PERU'S HUMAN RIGHTS IMAGE ABROAD.

4. U.S. POLICY. OUR INTERESTS ARE ENGAGED IN THE GOP'S EFFORTS TO OVERCOME PERU'S WORST ECONOMIC CRISIS SINCE THE WAR WITHOUT RESORT TO HEAVY REPRESSION AND IN THE MILITARY'S ANNOUNCED INTENTION TO TURN OVER POWER TO AN ELECTED CIVILIAN GOVERNMENT IN 1980. THE USG IN PURSUING THESE INTERESTS WILL HAVE TO CONSIDER DIRECT ASSISTANCE (PL-480 TITLE I) AND WHATEVER SUPPORT MAY BE POSSIBLE FOR PERU'S ATTEMPTS TO OBTAIN ADDITIONAL HELP FROM THE INTERNATIONAL FINANCIAL COMMUNITY. SHLAUDEMAN
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Message Attributes

Automatic Decaptioning: X
Capture Date: 01-Jan-1994 12:00:00 am
Channel Indicators: n/a
Current Classification: UNCLASSIFIED
Concepts: ECONOMIC REPORTS
Control Number: n/a
Copy: SINGLE
Sent Date: 10-Aug-1977 12:00:00 am
Decaption Date: 01-Jan-1960 12:00:00 am
Decaption Note:
Disposition Action: RELEASED
Disposition Approved on Date:
Disposition Case Number: n/a
Disposition Comment: 25 YEAR REVIEW
Disposition Date: 22 May 2009
Disposition Event:
Disposition History: n/a
Disposition Reason:
Disposition Remarks:
Document Number: 1977LIMA06741
Document Source: CORE
Document Unique ID: 00
Drafter: n/a
Enclosure: n/a
Executive Order: N/A
Errors: N/A
Expiration:
Film Number: D770288-0210
Format: TEL
From: LIMA
Handling Restrictions: n/a
Image Path:
ISecure: 1
Legacy Key: link1977/newtext/t19770877/aaaacnkj.tel
Line Count: 136
Litigation Code IDs:
Litigation Codes:
Litigation History:
Locator: TEXT ON-LINE, ON MICROFILM
Message ID: 78c9305d-c288-dd11-92da-001cc4696bcc
Office: ACTION ARA
Original Classification: LIMITED OFFICIAL USE
Original Handling Restrictions: n/a
Original Previous Classification: n/a
Original Previous Handling Restrictions: n/a
Page Count: 3
Previous Channel Indicators: n/a
Previous Classification: LIMITED OFFICIAL USE
Previous Handling Restrictions: n/a
Reference: 77 STATE 180067, 77 LIMA A-117, 77 LIMA 4852
Retention: 0
Review Action: RELEASED, APPROVED
Review Content Flags:
Review Date: 07-Apr-2005 12:00:00 am
Review Event:
Review Exemptions: n/a
Review Media Identifier:
Review Release Date: n/a
Review Release Event: n/a
Review Transfer Date:
Review Withdrawn Fields: n/a
SAS ID: 1648873
Secure: OPEN
Status: NATIVE
Subject: ECONOMIC ALERT REPORT - PERU
TAGS: ECON, EALR, PE
To: STATE
Type: TE
vdkgvwkey: odbc://SAS/SAS.dbo.SAS_Docs/78c9305d-c288-dd11-92da-001cc4696bcc
Review Markings:
Margaret P. Grafeld
Declassified/Released
US Department of State
EO Systematic Review
22 May 2009
Markings: Margaret P. Grafeld Declassified/Released US Department of State EO Systematic Review 22 May 2009